No. 12,760

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

CALIFORNIA STATE BOARD OF EQUALIZATION,

*Appellant,*

*vs.*

PAUL W. SAMPSELL, Trustee in Bankruptcy of the Estate of Twenty-nine Palms Air Academy, *et al.*,

*Appellee.*

---

## APPELLEE'S BRIEF.

---

FRANK C. WELLER,
HUBERT F. LAUGHARN,
THOMAS S. TOBIN,
817, 111 West 7th Street,
Los Angeles, California.
*Attorneys for Appellee.*



Parker & Company, Law Printers, Los Angeles. Phone MA. 6-9171.

## TOPICAL INDEX.

## TABLE OF AUTHORITIES CITED.

STATUTES PAGE

No. 12,760

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

California State Board of Equalization,
*Appellant,*

*vs.*

Paul W. Sampsell, Trustee in Bankruptcy of the Estate of Twenty-nine Palms Air Academy, *et al.*,
*Appellee.*

---

## APPELLEE'S BRIEF.

---

"If at first you don't succeed, try, try again." The writer of this Brief does not recall the author of this little aphorism, but in looking over the brief of the appellant, we cannot refrain from applying it to the case at Bar.

For many years the State Board of Equalization of California has been casting covetous eyes on property being liquidated in the Bankruptcy Courts under and by virtue of the Bankruptcy Acts enacted under the provisions of Article I, Section 8 of the Constitution of the United States. Repeatedly it has sought by one method or another, by filing claims, by threatening to subject Trustees to individual liability after their discharge, and appeals from the Courts of Bankruptcy in which the various estates were being administered and liquidated,

to impose the California State sales tax on the proceeds of liquidation sales.

In the case of the *State of California v. Moore, as Trustee for Paul Kent Truck Co.,* the State of California attempted without success to impose a tax penalty on William H. Moore, Jr. for gasoline tax on trucks claimed to have been sold by him in the bankruptcy liquidation of the Paul Kent Truck Co., and was rebuffed by this Court. (See *State of California v. Moore,* 88 F. 2d 564.) It next attempted to impose a sales tax on L. Boteler, as Trustee of the Estate of Davis Standard Bread Company, and after being enjoined by the District Court (*Matter of Davis Standard Bread Co.,* 46 Fed. Supp. 841), unsuccessfully appealed to this Court and was again rebuffed in its efforts. (*State Board of Equalization v. Boteler,* 131 F. 2d 386.) It then began warning trustees, who are statutory officers of the Court (Bankruptcy Act, Sec. 33), and receivers appointed by the United States District Court (Bankruptcy Act, Sec. 2-a, subd. 3), that unless they paid sales tax for carrying out their statutory duties (Bankruptcy Act, Sec. 47-a-1) they, officers of this Court, would be held personally liable after their discharge for unpaid sales taxes which the Board contended it had the power to levy and collect on liquidation sales for the *privilege* of carrying on the business of acting as statutory officers of the Federal Court under the provisions of the Bankruptcy Act.

Realizing that the failure of trustees to pay the taxes demanded was not a tortious liability, for which the trustees would be liable outside of their bonds, but would constitute a monetary liability for which their statutory bonds might be liable while in office (Bankruptcy Act, Sec. 50-b), and that after the distribution of the assets of the bank-

rupt estate to creditors, they would be placed at the mercy of the State Courts, involving a State tax for which they might be held personally liable, the Referees in Bankruptcy made orders requiring the State Board of Equalization, if it claimed any sales tax from the trustees in bankruptcy, arising from liquidation sales in bankruptcy, for what it deemed the privilege of fulfilling their office, to make its demands in the Bankruptcy Court while the estate was yet intact; and to have this taxing agency establish its expense of administration claim within a reasonable time or forever hold its peace. This did not constitute a suit against the State of California, as has been repeatedly asserted by the State Board of Equalization. (See *California State Board of Equalization v. Goggin,* 191 F. 2d 726, at page 728.)

While the case of *California State Board of Equalization v. Goggin* was pending, the State Board of Equalization filed a motion to set aside, vacate and dismiss the orders of the Referees so made in various pending bankruptcy proceedings.

As can be seen from an examination of the record, this motion involved numerous cases. They were all consolidated for hearing before Judge James M. Carter in the United States District Court for the Southern District of California. The State Board of Equalization appeared by the Attorney General's office, and the appellee here appeared by Hubert F. Laugharn. There was no dispute on the facts [R. p. 37], hence the record shows nothing but an oral argument on the right of the State to levy a sales tax on judicial sales in the Bankruptcy Court, and of the right of the Bankruptcy Court to protect its officers, either while the office or after their discharge, in connection with their official acts, or, as the

State Board of Equalization contends, an official omission while in office. Notwithstanding the fact that the appellant here was the moving party, it apparently offered no evidence as it now complains. (Appellant's Br. p. 3.) By tacit consent, the motion was argued as a pure question of law [R. p. 37] and was denied by Judge Carter. [R. p. 28.]

The appellant then applied to this Court for a writ of prohibition against Judge Carter and Judge McCormick of the United States District Court. (Appellant's Br. p. 4.) After argument here the writ of prohibition was denied without opinion.

Thereafter, on August 21, 1951, this Court handed down another opinion in *California State Board of Equalization v. Goggin,* 191 Fed. 726, affirming a restraining order entered by Judge Jacob Weinberger in the *West Coast Cabinet & Fixture Co.,* restraining the efforts of the State Board of Equalization to collect sales tax on some cabinets sold by the Trustee. The Opinion of the Court in that case followed *State Board of Equalization v. Boteler,* and the judgment of the District Court was affirmed. In a separate concurring Opinion filed by United States District Judge James Alger Fee, sitting on the Court at the time *California State Board of Equalization v. Goggin* was heard, Judge Fee vigorously condemned the practice of this State taxing agency to attempt to burden liquidation required under a federal law with a state tax. Judge Fee said:

> "A tax on this transaction, whatever form it takes, is a tax on the process of the Court liquidating assets in accordance with constitutional power. In

another aspect it may be considered as a license fee required of a federal officer to make liquidation. In either event it is void."

In arguing *State Board of Equalization v. Goggin* before this Court the writer of this brief concluded his oral argument with the statement that if the State of California could impose a tax or license fee on a trustee in bankruptcy, a statutory officer appointed by the United States District Court, to perform certain mandatory duties, then the State can likewise require the United States Marshal to take out a license to conduct each execution sale or a sale under a decree in admiralty on the ground that the United States Marshal was in the business of selling property of delinquent debtors under execution, or merchandise condemned for one reason or another by the Federal Courts. Judge Fee's special concurring opinion in the case of *Goggin v. State Board of Equalization* would seem to pursue very much the same line of reasoning.

Notwithstanding the setback received at the hands of this Court, the State Board of Equalization now has taken this appeal from Judge Carter's order affirming those of the Referees.

Citing no applicable authorities, the appellant, in its Opening Brief, resorts to sarcasm, which we believe ill-befits the high office of Attorney General of a sovereign state. The orders entered by the Referees and on review by the District Judge were orders entered under an express grant of jurisdiction under Section 2-a, subdivision

15, authorizing courts of bankruptcy to "make such orders, issue such process, and enter such judgments in addition to those specifically provided for, as may be necessary for the enforcement of the provisions of this Act; * * *."

Notwithstanding the fact that these orders were duly and legally entered in pending proceedings and given the stamp of approval by the District Court, throughout the entire brief filed on this appeal, appellant does not deign to dignify these orders as being such. Every reference, so far as we have been able to ascertain from a careful examination of appellant's brief, refers to the results of these judicial proceedings as "orders." The quotation marks are as eloquent as if counsel for the appellant had resorted to the appellation of "alleged" orders or "so-called" orders in referring to the orders of the Referee and the District Judge. Frankly, we believe such contemptuous language to be as overzealous as it would be if a private attorney appealed from a judgment based on the verdict of a jury in the United States District Court, after a contested trial, and referred to it as a "judgment" based on a "verdict" of a "jury."

Here there is involved only a serious question of law which has been repeatedly determined by this Court against the appellant, and we don't believe that the sneering reference to the lower court's "orders" will lend any assistance to this Court in again determining that the State Board of Equalization of California is wrong.

## Has the Court an Inherent Right to Protect Its Own Officers in Carrying Out Their Mandatory Duties After They Are Discharged and the Estate Distributed Beyond Redemption?

It is clear that the trustees, acting as officers of the Court, were facing a clear and immediate danger. They were between two fires. Section 47-a of the Bankruptcy Act required them to convert into cash the property of the estates for which they were trustees under the direction of the Court, and to close up the estates as expeditiously as is compatible with the best interests of the parties in interest, and to disburse the money only by check or draft on such depositories, and to examine all proofs of claim and object to the allowance of claims that may be improper, and to pay dividends within ten days after they are declared by Referees, and make reports both interlocutory and final to the courts during the course of the administration. In carrying out the duty to object to claims or demands made against a bankrupt estate, it is patently necessary that the Trustee know the amount and nature of such claims or demands. It is also necessary for the Trustee to bring before the Referee for approval the various expenses of administration for approval or disapproval. (*Matter of California Pea Products Inc.,* 37 Fed. Supp. 638.) Such was the nature of the sales tax claimed here. The State Board of Equalization reserved unto itself the right to withhold such alleged expense of administration obligations, and if the Trustee did not seek them out and pay them, to hold him personally liable after he was discharged, after his office had ceased to exist, and after he was out from under the protection of the Court which appointed him and directed him in his duties.

In other words, he would close any estate for which he had been Trustee and in which all assets had been sold and distributed under the mandate of Section 47-a of the National Bankruptcy Act, at his peril of having a demand made upon him for payment of a sales tax, on assets sold by him as an officer of the Court, which tenure of office was now terminated, and of being compelled to go out and at his own expense employ private attorneys, pay filing fees for an answer in the State Court, and if he desired a jury trial on the demands of the State Board of Equalization, post one day's jury fees and mileage to exercise his constitutional right to a trial by jury.

Considering the modest fees allowed to a Trustee under Section 48-a of the National Bankruptcy Act, it is very evident that no person could be found, who would undertake the onerous and complex duties imposed upon trustees in bankruptcy under Section 47 of the Naitonal Bankruptcy Act, at his personal peril of having to defend against suits and possibly personal judgments against him individually, imposed by the courts of the State of California for merely carrying out the mandatory duties imposed upon him by the Federal Court. If the estate were a large one involving several hundred thousands of dollars, the sales tax demanded would be correspondingly large and the Trustee's compensation would diminish to a maximum of 1% of all sums realized from liquidation sales over a total of $10,000.00. (Bankruptcy Act. Sec. 48-c, subd. 1.) It being evident to any sensible man that no qualified person except an execution-proof ne'er-do-well would even consider accepting a trusteeship in bankruptcy in the face of such imminent danger, the lower court in the interests of efficient administration of bankrupt estates, and in the face of the threatening attitude

of a State Bureau to impose a penalty on trustees for conscientiously performing their mandatory duties, threw a mantle of protection over Mr. Sampsell, Mr. Goggin and others who had earned the trust and confidence of the courts by their past able administrations over a period of years. The Court reassured them that the court that appointed them would stand behind them after their discharge and would not permit any state bureau to impose a penalty on them for ministerial acts performed by them, after it had discharged them and exonerated their faithful performance bonds.

The Referees in bankruptcy and the District Judges by their orders leave no doubt as to whether or not the Trustee should have the protection of the Court. Certainly such protection is warranted not only under the provisions of Section 2-a, subdivision 15, but by repeated decisions of this Court, reassuring trustees that they would be protected after their discharge from vexatious and expensive suits brought by a disappointed state taxing agency against them individually. We respectfully submit that not only as a matter of discretion, but as a matter of right, if not as a mandatory duty, the District Court entered these orders protecting its trustees from danger after their discharge.

In referring to the contended sales taxes against the trustees, District Judge Paul J. McCormick, *In the Matter of California Pea Products, Inc.*, 37 Fed. Supp. 638, said:

> "The transactions upon which the state bases its contention in this review have all taken place after adjudication and the selection of the trustee in bankruptcy. The claims may therefore be considered as not strictly 'claims' against the estate within the contemplation of sections 57(n) and 64(a), but

rather an expense of administration provided for in section 62 of the Act. But the same power of adjudicating such 'claims' is vested in the bankruptcy court by section 62 as in the matter of tax claims under sections 57(n) and 64(a).

"The Supreme Court in *Kalb v. Feuerstein,* 308 U. S. 433, 41 Am. B. R. (N. S.) 501, speaking of the broad and plenary power of courts of bankruptcy said, 'The Constitution grants Congress exclusive power to regulate bankruptcy and under this power Congress can limit the jurisdiction which courts, state or federal, can exercise over the person or property of a debtor who duly invokes the bankruptcy law.' See, also, Arkansas Corporation Commission v. Thompson (C. C. A. 8th Cir.), 44 Am. B. R. (N. S.) 536, 116 F. (2d) 179.

* * * * * *

"We conclude by holding that the findings, injunction and order of the referee, dated March 22, 1940, are modified as follows: The State Board of Equalization of the state of California, its officers, agents, employees and attorneys are, and each of them is, enjoined and restrained from in any manner enforcing or attempting to enforce any claim, tax, assessment, collection, penalties or sanctions provided in or pursuant to Act 8493 of the General Laws of the state of California against the estate of *California Pea Products, Inc.,* a corporation, bankrupt, or against the trustee thereof, or against L. Boteler personally, or against any property of said bankrupt, or of L. Boteler, or from in any manner interfering with the administration of this estate, without prejudice, however, to the presentation and filing of any claim for taxes by the State Board of Equalization of the state of California, its accredited

and authorized officers, agents or attorneys, within the time allowed by law, and to having such claim considered by the referee and its legality and validity determined by him, or without prejudice to a 'bar order' of the referee."

This Court recognized the problem which confronted the Court (the Referee or the District Court) which had before it the administration of bankrupt estates, and on this same problem in *McColgan v. Maier Brewing Co.*, 134 F. 2d 385, Judge Healy, who wrote the opinion for the Court, said:

"In June, 1932, an involuntary petition was filed against Maier Brewing Company and a receiver appointed with authority to manage and operate the business and property of the alleged bankrupt. The receiver and his successor, the latter being appointed in 1935, operated the business until September 10, 1938. Appellant, Franchise Tax Commissioner of the state of California, asserts that during this period franchise taxes based on net income were assessable under the state Bank and Corporation Franchise Tax Act, Stats. 1929, p. 19, as amended.

"Each year, except in 1935, taxable net income was derived by the receivers from their operation of the brewery. Although the receivers paid federal taxes on this income they paid to the state only the minimum tax of $25.00, presumably in the belief that since the corporation itself was inactive, the franchise tax was not owing. * * *

"The taxes accruing as a consequence of the operation of the business by the receivers were expenses of administration. They were not provable debts owing by the corporation itself; but were obligations of the receivership. In respect of the payment of administrative expenses, the statute (11 U. S. C. A., Sec.

102, sub. a) provides that unless other provisions for their payment are made they shall be 'reported in detail, under oath, and examined and approved or disapproved by the Court. If approved, they shall be paid or allowed out of the estates in which they were incurred.' No other provision was made for the payment of these expenses. Thus the liability of the estate was dependent upon their being reported and their payment directed by Court order.
* * *

"Of course if these taxes had been assessed and a claim made upon the receivers for their payment they would, like administrative expenses generally, have occupied a preferred status. *But the statute does not dispense with the necessity for making timely demand for their payment in the receivership proceeding.* As much now as in the past orderly procedure requires that *administrative expenses be settled while the property yet remains in the custody of the Court.*" (Italics ours.)

Not satisfied to abide by the plain, unequivocal decision of this Court in *State Board of Equalization v. Boteler,* 131 F. 2d 386, someone then induced the State Legislature to amend the Sales and Use Tax Act to include, in so many words, "Trustees in Bankruptcy," and the merry-go-round of litigation started all over again, winding up in this Court in *California State Board of Equalization v. Goggin,* 191 F. 2d 727.

The requirement of the State Board of Equalization that trustees take out licenses to perform their mandatory duties and to make special reports to the State Board of Equalization, where purely liquidation sales were involved, imposes additional burdens upon a trustee in bankruptcy in conflict with Federal law and is unconstitutional.

This question was argued in our brief in *State Board of Equalization v. Boteler,* No. 10,021 in this Court, 191 F. 2d 726. In that case we cited:

*Holmes v. Rowe,* 97 F. 2d 537;

*In re Brinn,* 262 Fed. 527;

*Donnelly v. Southern Pacific Co.,* 18 Cal. 2d 863;

*Moore v. Bay,* 284 U. S. 4.

in response to the contention that the Trustee was not entitled to injunctive relief and that he had a plain, speedy and adequate remedy at law by suing to recover taxes paid, in the State Courts. We called attention of the Court to the right of the Federal Courts to enjoin enforcement of an unconstitutional State statute by State officers clothed with authority to enforce it where it violates the Federal statute, and cited:

*Tyson & Brothers United Theatre Ticket Officers v. Banton,* 273 U. S. 418;

*Pennsylvania v. West Virginia,* 262 U. S. 553;

*Fox Film Corpn. v. Trumbull,* 7 F. 2d 715;

*McNaughton v. Johnson,* 242 U. S. 344;

*Claybrook v. City of Owensboro,* 16 Fed. 297;

*Wells Fargo & Co. v. Taylor,* 254 U. S. 175;

*Caldwell v. Sioux Falls Stockyard Co.,* 242 U. S. 559;

*Van Deman & Lewis Co. v. Rast,* 214 Fed. 827;

*Yee Gee v. City & County of San Francisco,* 235 Fed. 757;

*Pierce v. Society of the Sisters,* 268 U. S. 510;

*Wofford Oil Co. v. Smith,* 263 Fed. 396;

*Minneapolis Brewing Co. v. McGillivray,* 104 Fed. 258.

## Conclusion.

We respectfully submit that the order of the District Court in these cases should be affirmed, and affirmed in such a way and in such unequivocal language as to terminate the running battle that has been going on between the State Board of Equalization and other California taxing agencies continuously since 1941, when Judge McCormick handed down his original decision in the matter of *California Pea Products, Inc., Bankrupt,* 37 Fed. Supp. 638, and under cover of which, by one device or another, the State Board of Equalization has been endeavoring to intrude into and encroach upon the field of bankruptcy administration and liquidation, a field essentially federal. We believe that the decision in this case should follow the law as laid down in *State Board of Equalization v. Goggin,* 191 F. 2d 726, be as unequivocal as was the special concurring Opinion of District Judge Fee. The very caption of the case at bar indicates clearly the large number of bankrupt estates which are being held open by one Trustee alone because he dared not close them and endanger his own personal fortune in interminable litigation in the state courts. Mr. Sampsell is not the only Trustee who has been confronted by this dilemma. Mr. Goggin and Mr. Boteler have both been compelled to face the express or implied threat that unless they paid sales tax to the State of California on mandatory liquidation sales conducted in a Federal Court they would be held personally liable to the State of California for their alleged dereliction of duty. We do not know how many hundreds of thousands or possibly millions of dollars are lying idle in designated depositories of Bankruptcy Courts awaiting the final clarifying word from this Court to release them. If the Trustees involved release them in

dividends, as said before, they are facing the imminent danger of being personally sued for sales tax for the *privilege* of carrying on the business of being duly elected officers of the Bankruptcy Court under Section 33 of the National Bankruptcy Act.

The theory on which the appellant is now seeking to impede bankruptcy administration, unless paid their price, is that individuals who accept two or more trusteeships in bankruptcy a year are engaged in the business of being trustees in bankruptcy and are subject to state taxation under the California Sales and Use Tax Laws. We believe that such a contention is utterly ridiculous. Simply because there are men in the State of California who by reason of education, experience, qualifications and skill are entrusted by the courts in the Northern and Southern Districts of California with the administration of numerous complicated bankrupt estates, we do not believe that any state agency has a right constitutionally to invade the indisputably federal field of bankruptcy administration and declare by bureaucratic ukase that Federal Court officers are engaged in the "business of trustee in bankruptcy."

We respectfully submit that the order of Judge Carter affirming the Referee's bar orders in these cases, and each of them, should be affirmed.

Respectfully submitted this 18th day of December, 1951.

FRANK C. WELLER,
HUBERT F. LAUGHARN,
THOMAS S. TOBIN,
*Attorneys for Appellee.*